

1 JAMES L. LOPES (No. 63678)  
2 JEFFREY L. SCHAFER (No. 91404)  
3 SARAH M. KING (No. 189621)  
4 HOWARD, RICE, NEMEROVSKI, CANADY,  
5 FALK & RABKIN  
6 A Professional Corporation  
7 Three Embarcadero Center, 7th Floor  
8 San Francisco, California 94111-4065  
9 Telephone: 415/434-1600  
10 Facsimile: 415/217-5910

11 Attorneys for Debtor and Debtor in Possession  
12 PACIFIC GAS AND ELECTRIC COMPANY

13 UNITED STATES BANKRUPTCY COURT  
14 NORTHERN DISTRICT OF CALIFORNIA  
15 SAN FRANCISCO DIVISION

16 In re

17 PACIFIC GAS AND ELECTRIC  
18 COMPANY, a California Corporation,

19 Debtor.

20 Federal I.D. No. 94-0742640

No. 01 30923 DM

Chapter 11 Case

Date: May 16, 2001

Time: 9:30 a.m.

Place: 235 Pine St., 22nd Floor  
San Francisco, California

HOWARD  
RICE  
NEMEROVSKI  
CANADY  
FALK  
& RABKIN  
A Professional Corporation

21 MEMORANDUM OF POINTS AND AUTHORITIES IN SUPPORT OF  
22 DEBTOR'S MOTION FOR AUTHORITY TO HONOR ITS  
23 OBLIGATIONS FOR PUBLIC PURPOSE PROGRAMS

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MPA IN SUPPORT OF MOT. TO HONOR OBLIGATIONS UNDER PUBLIC PURPOSE PROGRAMS

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WD 042401/1-1419901/gff/910708/v9

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I.

INTRODUCTION

Pacific Gas and Electric Company, the debtor and debtor in possession in the above-captioned Chapter 11 case (the "Debtor" or "PG&E"), submits this Memorandum of Points and Authorities In Support of Debtor's Motion For Authority To Honor Its Obligations For Its Public Purpose Programs pursuant to Bankruptcy Code Sections 541(d) and 105 (the "Motion"). In a nutshell, PG&E by the Motion seeks authorization to continue uninterrupted with a range of energy efficiency-related programs and related activities (collectively the "Public Purpose Programs") that are legislatively mandated and that are fully funded by a special surcharge paid by all ratepayers. Because PG&E is effectively a conduit of the moneys collected and used for funding the Public Purpose Programs, PG&E believes such funds are not property of PG&E's bankruptcy estate and PG&E therefore should not need any Bankruptcy Court authorization to proceed to honor its obligations in connection with the Public Purpose Programs. Nonetheless, because part of the Public Purpose Programs, as described more fully below, involve PG&E's hiring and payment of various vendors and contractors to fulfill the mandates of the Public Purpose Programs, and because PG&E seeks to pay all amounts owing to such vendors and contractors on account of pre-petition goods and services, PG&E out of an abundance of caution is disclosing all pertinent facts and seeking the Court's authorization to so proceed with its Public Purpose Programs. The effect of a favorable ruling on the Motion is that (i) PG&E will have unambiguous authority to pay approximately \$19.2 million in pre-petition invoices and another approximately \$17.9 million in anticipated invoices net yet received, in ease case either from vendors and contractors who supplied goods and services pre-petition in connection with the Public Purpose Programs or from customers who became entitled to rebates pre-petition in connection with the Public Purpose Programs, and (ii) the approximately \$260 million currently booked in the energy efficiency programs balancing accounts described below will continue to be set aside for payment for energy efficiency obligations that constitute part of the Public Purpose Programs.

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1 II.

2 GENERAL BACKGROUND

3 PG&E is an investor-owned utility providing electric and gas services to millions  
4 of California residents and businesses. Beginning approximately last summer, as a result of  
5 the partial deregulation of the power industry, PGE was forced to pay dramatically increased  
6 wholesale prices for electricity, but has been prevented from passing these costs on to retail  
7 customers, resulting in a staggering financial shortfall. In the face of the deterioration in  
8 PG&E's financial condition and with little progress having been made toward a resolution of  
9 the crisis, PG&E by early April 2001 determined that a Chapter 11 reorganization offered the  
10 best prospects for protecting the interests of its customers, creditors, employees and  
11 shareholders alike. Accordingly, PG&E filed a voluntary petition under Chapter 11 of the  
12 Bankruptcy Code on April 6, 2001. PG&E continues to manage and operate its business and  
13 property as a debtor in possession pursuant to Sections 1107 and 1108 of the United States  
14 Bankruptcy Code (11 U.S.C. §§1107-1108). No trustee has been appointed.

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16 III.

17 PG&E'S PUBLIC PURPOSE PROGRAMS<sup>1</sup>

18 The Public Purpose Programs that pertain to the Motion include a range of energy  
19 efficiency, low-income energy efficiency, research and development, and renewable energy  
20 generation programs, all as described more particularly in this Section III.

21 PG&E has been offering ratepayer-funded energy efficiency and low-income  
22 energy efficiency programs to its customers since at least 1976. (PG&E's low-income  
23 energy efficiency program hereinafter is referred to as the "Low-Income Energy Efficiency  
24 Program," PG&E's energy efficiency programs other than the Low Income Energy  
25 Efficiency Program hereinafter are referred to as the "regular Energy Efficiency Programs,"

26  
27 <sup>1</sup>The Declaration of Steven J. McCarty (hereinafter referred to as the "McCarty Declaration" and cited as the  
28 "McCarty Decl.") submitted concurrently herewith provides support for the factual matters set forth in this Section III.

1 and PG&E's Low-Income Energy Efficiency Program and regular Energy Efficiency  
2 Programs hereinafter are collectively referred to as the "Energy Efficiency Programs.") The  
3 Energy Efficiency Programs have always been designed to provide financial incentives to  
4 individuals, businesses, vendors, retailers, wholesale distributors or manufacturers to install,  
5 sell or manufacture more efficient energy-using equipment than customers would normally  
6 install in the absence of the program. The Energy Efficiency Programs also are intended to  
7 educate consumers about the benefits of purchasing energy efficient equipment and using  
8 energy-conserving practices. The objective has always been that if cost-effective energy  
9 efficiency products are used, less of our scarce energy resources will be depleted, to the  
10 benefit of both society and the purchaser of the energy-saving equipment. Today, with the  
11 high cost and looming shortages of energy, energy efficiency is more important and more  
12 cost-effective than ever. McCarty Decl., ¶2.

13 The Low-Income Energy Efficiency Programs install energy efficiency measures  
14 in the homes of qualified low-income households, at no charge to the participant. The Low-  
15 Income Energy Efficiency Programs are authorized by Section 2790 of the Public Utilities  
16 Code Section 2790. In addition to educating the participants about energy efficiency and  
17 saving energy, the Low-Income Energy Efficiency Program is also designed to reduce  
18 hardships and increase comfort in the participating low income homes. *Id.* ¶3.

19 Prior to 1997, the California Public Utilities Commission (the "CPUC")  
20 authorized the Energy Efficiency Programs and the funding levels associated with the  
21 programs. The portion of the funds received from customers' bills that were allocated to the  
22 Energy Efficiency Programs were debited to the balancing accounts established for the  
23 programs, and the costs of the programs were credited to the accounts.<sup>2</sup> In this particular  
24 instance, the balancing accounts were used as an administrative convenience to assure PG&E

25  
26 <sup>2</sup>Balancing accounts are regulatory mechanisms designed to track and match specific costs and/or revenues for a  
27 variety of reasons, including but not limited to the following: to eliminate or change profit incentives for certain  
28 expenditures, to manage volatile costs, to finance costs for ratepayers over longer time periods, to manage incentive  
programs, or, as in this instance, to ensure funding for particular programs.

1 and the CPUC that the funds authorized for the programs were spent only on the programs.  
2 Approximately every three years, PG&E would submit an accounting of the status of the  
3 balancing accounts, and propose whether any overcollections in the account at that time  
4 should be carried over to future Energy Efficiency Programs or refunded to PG&E's  
5 ratepayers. Also during the same period prior to 1997, PG&E conducted certain research  
6 and development activities (the "Research and Development Program") that were subject to  
7 the same balancing account and refund/carryover treatment. Id. ¶4.

8 In 1996, in order to ensure that the funds for Public Purpose Programs "are not  
9 commingled with other revenues," the California Legislature enacted Sections 381 and 382  
10 of the Public Utilities Code that established a separate electric rate "component" or surcharge  
11 for what the Legislature termed "Public Purpose Programs," encompassing mandated Low-  
12 Income Energy Efficiency Programs, regular Energy Efficiency Programs, Research and  
13 Development Programs, and Renewable Energy Generation Programs. This Public Purpose  
14 Programs surcharge applied and continues to apply to all customers.<sup>3</sup> Section 381(c) requires

15 <sup>3</sup>Section 381 provides in part:

16 381. (a) To ensure that the funding for these programs described in subdivision (b) and Section 382 are not  
17 commingled with other revenues, the commission shall require each electrical corporation to identify a separate rate  
18 component to collect the revenues used to fund these programs. The rate component shall be a nonbypassable element  
19 of the local distribution service and collected on the basis of usage. This rate component shall fall within the rate levels  
20 identified in subdivision (a) of Section 368.

21 (b) The commission shall allocate funds collected pursuant to subdivision (a), and any interest earned  
22 on collected funds, to programs which enhance system reliability and provide in-state benefits as follows:

- 23 (1) Cost-effective energy efficiency and conservation activities.
- 24 (2) Public interest research and development not adequately provided by competitive and  
25 regulated markets.
- 26 (3) In-state operation and development of existing and new and emerging renewable resource  
27 technologies defined as electricity produced from other than a conventional power source within the meaning of Section  
28 2805, provided that a power source utilizing more than 25 percent fossil fuel may not be included.

Section 382 provides in relevant part:

382. Programs provided to low-income electricity customers, including, but not limited to, targeted energy-  
efficiency services and the California Alternative Rates for Energy Program shall be funded at not less than 1996  
authorized levels based on an assessment of customer need. The commission shall allocate funds necessary to meet the  
low-income objectives in this section.

In a decision issued in February 1997, the CPUC ordered the funding levels for the Public Purpose Programs to  
be funded at the minimum levels set forth in Sections 381 and 382, which was consistent with funding in previous years.

(continued . . .)

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PG&E to "collect and spend" the funds in accordance with the statute. *Id.* ¶5.

Subsections 381(c)(1) and (3) specifically require PG&E to fund the regular *electric* Energy Efficiency Programs at an amount not less than \$106 million per year, Research and Development Programs at \$30 million per year, and Renewable Energy Generation Programs at \$48 million per year.<sup>4</sup> The \$30 million for Research and Development Programs and \$48 million for Renewable Energy Generation Programs are required to be collected by PG&E from ratepayers and transferred quarterly to the California Energy Commission (the "CEC"), which is responsible for implementing the programs for those two areas. PG&E's electric Low-Income Energy Efficiency Program is currently funded at approximately \$14 million per year.<sup>5</sup> *Id.* ¶6.

*Natural gas* regular Energy Efficiency Programs, Low-Income Energy Efficiency Programs, and Research and Development Programs, which have also been ongoing since at least 1976, also became subject to a separate surcharge in customer rates when Sections 890-900 of the Public Utilities Code became effective on January 1, 2001. For the *natural gas* programs, PG&E is required to surcharge and collect the specified Public Purpose Programs revenues and submit the amounts collected to the State Board of Equalization at the end of each quarter, which then distributes the money in accordance with allocations determined by the CPUC. For 2001, PG&E is collecting \$17.1 million in natural gas revenues for regular Energy Efficiency Programs, \$15 million for natural gas Low-Income Energy Efficiency Programs, and \$1.9 million for gas Research and Development Programs, all of which are also consistent with funding in past years. *Id.* ¶7.

Each year, PG&E submits filings to the CPUC for approval of both electric and

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(... continued)

Decision 97-02-014, 70 CPUC 2d 774. The funding levels have not changed since that time.

<sup>4</sup>Section 381(c) requires these expenditures through the year 2001. The Legislature has extended these requirements for additional years, however. See Public Utilities Code Section 399.8, effective January 1, 2001.

<sup>5</sup>The California Alternative Rates for Energy Program, required by Section 739.1 of the Public Utilities Code, is also considered a Public Purpose Program. It offers a 15% discount on energy costs for qualifying low-income customers. Since it takes the form of a discount, there is no explicit funding level for this program, other than the costs of administering the program. Instead, PG&E receives less revenue from the participating customers.

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1 natural gas regular Energy Efficiency and Low-Income Energy Efficiency Programs and  
2 expenditures for the coming fiscal year.<sup>6</sup> PG&E's 2001 Energy Efficiency Programs  
3 application, which requested approval of a total Energy Efficiency Programs budget of \$156  
4 million for 2001 (including both gas and electric energy efficiency and conservation  
5 programs, plus money collected in previous years but not yet spent), was approved by the  
6 CPUC on January 31, 2001. PG&E's 2001 Low-Income Energy Efficiency Program was  
7 approved through the end of 2001 in a decision adopted in July 2000. All of the payments  
8 that PG&E seeks authority to make, therefore, will be made pursuant to Energy Efficiency  
9 Programs required by the Public Utilities Code and specifically analyzed and approved by  
10 the CPUC. *Id.* ¶8.

11 Under the legislation imposing the surcharge, PG&E has a statutory obligation to  
12 "collect and spend" the funds enumerated for the Public Purpose Programs, including the  
13 Energy Efficiency, Research and Development and Renewable Energy Generation Programs.  
14 As such, PG&E is required to pass through to the beneficiaries of the Public Purpose  
15 Programs the funds specifically collected and allocated for the programs.<sup>7</sup> The funds for the  
16 programs have been consistently funded for years and specifically earmarked for the  
17 intended programs, with no discretion for PG&E to apply the funds to other purposes.<sup>8</sup> *Id.*

18  
19 <sup>6</sup>Since the California Energy Commission administers the Research and Development Program and the  
Renewable Energy Generation Program, it determines the budget and parameters for those programs.

20 <sup>7</sup>Indeed, in the decision approving the 2001 Energy Efficiency Programs, the CPUC went so far as to say: "The  
21 funds collected and earmarked for the Program Year 2001 energy efficiency programs shall be held by the utilities in  
22 trust for the benefit of the commission and spent solely in accordance with the budgetary and other requirements set  
23 forth herein and shall not be used for any other purpose(s) whatsoever." – Decision 01-01-060, issued February 5, 2001,  
24 Ordering Paragraph 5, at *mimeo* page 42. While the CPUC's statement that the Public Purpose Programs funds are held  
in trust "for the benefit of the commission" is technically incorrect in that such funds clearly are to be held and  
expended for the benefit of the beneficiaries of the Public Purpose Programs by the California Legislature's and the  
CPUC's own mandate, the CPUC no doubt was intending to emphasize the special nature of the Public Purpose  
Programs surcharge and resulting funds.

25 <sup>8</sup>In stark contrast to the Public Purpose Programs which have always received full funding in rates, in recent  
26 months the CPUC has ordered PG&E to institute new programs, at costs of hundreds of millions of dollars annually,  
27 without providing any additional funding. For example, in a recent decision issued March 29, 2001, (Decision 01-03-  
073), the CPUC ordered PG&E to commence two new programs, expected to cost \$63 million per year for four years,  
28 without providing any new electric revenues to pay for the programs. Decision 01-03-073, Ordering Paragraph 2, at  
*mimeo* page 48. Indeed, CPUC's order purporting to require PG&E to pay new costs without providing adequate new  
funding in rates contributed to PG&E's decision to seek reorganization under Chapter 11 of the Bankruptcy Code.

¶9. They are for all practical purposes simply a passthrough of funds collected specifically for that purpose.

Section 381(a) of the Public Utilities Code requires each relevant utility to identify a separate rate component for the Public Purpose Programs. Accordingly, since early 1998, after allowing an approximately one-year period to conform PG&E's billing/invoicing systems and software to reflect the mandates of the legislation imposing the nonbypassable surcharge for Public Purpose Programs, all monthly bills to PG&E's approximately 4.7 million customers have reflected the surcharge as a separate line item entitled "Public Purpose Programs" in the account detail portion of the bill, which surcharge is computed based on a fixed charge per kilowatt-hour consistent with the legislation. Id.

¶10.

By the Motion, PG&E seeks to honor its obligations pursuant to its various specific Energy Efficiency Programs, as well as the passthrough of the Research and Development and Renewable Energy Generation funds to the CEC. This includes various payments by PG&E in connection with the pre-petition period, i.e., paying an estimated \$37.1 million in invoices to Energy Efficiency Programs vendors and contractors who supplied goods and services pre-petition, as well as paying the pre-petition portion of the passthrough to the CEC of the Research and Development and Renewable Energy Generation funds. Because of the energy crisis that precipitated this bankruptcy filing, both PG&E and the energy efficiency community have been working particularly hard on getting as much of the Energy Efficiency Programs results in place prior to this summer's electric peaks. As a result, an extraordinary amount of work had been completed but not yet paid for and/or invoiced at the time of the bankruptcy filing. Id. ¶11.

General descriptions of the majority of the Energy Efficiency Programs and their current status are described below:

1           A.   Rebate Programs.

2           PG&E has implemented a number of programs that provide rebates to consumers,  
3 vendors, designers and others in an effort to encourage use of energy efficient products. In  
4 2000, PG&E paid approximately \$22 million in rebates and vouchers pursuant to these  
5 programs. PG&E estimates that it currently owes approximately \$22.8 million to customers,  
6 retailers and others pursuant to rebate and voucher applications mailed pre-petition in 2001,  
7 and another approximately \$3 million in contractual payments to vendors and customers who  
8 have already installed the energy-saving measures that form the basis for the payments.  
9 PG&E has received invoices, which are now unpaid, of approximately \$14.4 million for  
10 these programs, and estimates that another \$11.5 million of work performed prior to the date  
11 of the bankruptcy filing, but not yet invoiced, remains to be invoiced to PG&E. *Id.* ¶12. The  
12 following are some salient examples of these rebate/incentive programs:

13           1.   Comfort Home. This program provides a financial incentive to residential  
14 builders and homebuyers for the installation of energy-efficient systems in new homes.  
15 Builders qualify for rebates by building specific features that save homeowners up to 25% in  
16 energy costs each month in comparison to standard new homes. Each home must feature  
17 high efficiency air conditioning, a tightly sealed duct system, and a natural gas range and  
18 dryer stub. Bonus payments are given for energy efficient window upgrades. PG&E also  
19 provides financial incentives to third party consulting firms who assist PG&E to market this  
20 program to residential builders. *Id.* ¶13.

21           2.   ENERGY STAR™ Showcase Homes. This program provides financial  
22 incentives for builders who construct homes that comply with the U.S. Department of  
23 Energy's ENERGY STAR™<sup>9</sup> standards for new homes. *Id.*

24           3.   Savings By Design. This program provides financial incentives to designers  
25 who complete high-performance commercial building design, construction and retrofit.

26 \_\_\_\_\_  
27           <sup>9</sup>ENERGY STAR™ is a trademark designed by the Department of Energy to assist consumers in choosing energy-  
28 efficient appliances and energy systems. The trademark allows consumers to make environmentally sound choices  
without having to educate themselves regarding the technical elements contributing to efficiency.

1 PG&E also offers design assistance and analysis through this program. Id.

2 4. Residential Appliance Rebates. This rebate programs offers direct customer  
3 rebates for ENERGY STAR™ qualified clothes washers, dishwashers, room air conditions,  
4 portable evaporative coolers, and refrigerators. Id.

5 5. 1-2-3 Cashback. This new residential rebate program was designed to make  
6 home improvements as easy as possible for customers. The program includes energy  
7 efficiency measures such as whole house fans, advanced whole house evaporative coolers,  
8 high performance dual-paned windows and ENERGY STAR™ programmable thermostats. Id.

9 6. Residential Contractor Program. This program helps customers reduce the  
10 cost of installing energy-efficient products and contracting for energy-saving services in their  
11 homes. PG&E provides customers with vouchers that may be given to participating  
12 contractors in partial payment for such installations as high-performance windows,  
13 programmable thermostats, insulation, ENERGY STAR™ central air conditioners, water  
14 heaters, and furnaces and heat pumps. The vouchers may also be used for such services as  
15 duct testing and sealing. Eligible contractors then submit the vouchers to PG&E for  
16 reimbursement. Id.

17 7. Standard Performance Contracts. This program provides financial  
18 incentives to large and small businesses and third parties that implement energy efficient  
19 measures that result in verified energy savings. The program pays up to \$2.0 million per  
20 corporate parent and \$500,000 per site for verified energy savings and demand reduction.  
21 Additional incentives are given to those measures that produce peak demand reductions. Id.

22 8. Express Efficiency Programs. The Express Efficiency Program provides cash  
23 rebates to encourage customers to plan, finance and install new energy-saving equipment.  
24 Consumers, retailers and wholesale distributors are each eligible to receive rebates under this  
25 program of up to \$25,000. Motor Express Efficiency provides rebates to approved  
26 distributors of energy efficient motors. Heating, Ventilating and Air Conditioning (HVAC)  
27 Express Efficiency provides rebates of \$5 per ton to approved distributors of energy-efficient  
28 air conditioning package units. Id.

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1           9. Power Savings Partners. In the mid-1990's, the CPUC authorized PG&E to  
2 conduct bids for energy efficiency vendors and customers to bid on the provision of energy  
3 efficiency resources. The bids were conducted and contracts signed, which have now been  
4 largely completed. Payment under the contracts was for verified, delivered energy savings,  
5 which are paid over a multi-year period as the energy-saving measures are determined to  
6 remain in place and operating. Payments are due this year and each of the next several years  
7 under these contracts. Id.

8           PG&E also incurs obligations to third-party administrators for its rebate  
9 programs. PG&E's Marketing Processing Center, for example, supports the rebate programs  
10 by performing such services as tracking rebate applications and payments, compiling a  
11 database for the programs, responding to requests for information, and verifying that  
12 applicants have implemented the energy saving measures. Last year, PG&E expended  
13 approximately \$1.2 million for these third-party services. PG&E estimates that the total pre-  
14 petition obligation in 2001 to these administrators amounts to approximately \$200,000.  
15 McCarty Decl. ¶14.

16           In addition, PG&E outsources some of its rebate programs to vendors. Under this  
17 type of arrangement, a vendor will market and pay rebates for approved energy efficient  
18 products and then seek reimbursement from PG&E. Participating vendors sometimes  
19 receive additional incentive payments in exchange for these services. PG&E paid  
20 approximately \$14 million to reimburse and compensate vendors for the rebate programs  
21 they offered on PG&E's behalf in 2000. Finally, PG&E estimates that it currently owes over  
22 \$2.8 million on invoices received from San Diego Gas & Electric Company and Southern  
23 California Edison Company pursuant to co-funding agreements supporting statewide Energy  
24 Efficiency Programs. Id. ¶15.

25  
26       B. Professional Consulting Programs.

27           PG&E has implemented programs that provide professional consulting services to  
28 customers who desire to improve energy efficiency. The following noteworthy examples of  
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1 some of these programs:

2 1. Energy Design Resources. This program provides design professionals with a  
3 readily available, integrated package of design performance tools, techniques, information,  
4 and educational resources facilitating the design and construction of energy efficient new  
5 buildings. Id. ¶16.

6 2. Industrial and Agricultural New Construction Program. This program  
7 provides industry-specific energy benchmarking studies to high-growth industries such as  
8 refrigerated warehousing, biotech, high tech, and wastewater treatment. The studies allow  
9 customers to identify and design new systems and facilities using the least energy and  
10 drawing the least demand over their useful lives. Id.

11 3. Energy Design Success. This program offers design assistance to industrial  
12 and agricultural customers to promote the installation of premium-efficiency new equipment  
13 and systems. The program also teaches customers to reduce energy costs and demand  
14 through the proper operation and maintenance of such equipment. Id.

15 Including support for these specific programs, PG&E has issued approximately  
16 115 contract work authorizations for professional services in the technical, marketing,  
17 advertising and policy evaluation areas. Additional activities undertaken pursuant to these  
18 contracts include studies, classes, evaluations and consultations on energy efficient lighting,  
19 heating, thermal systems, refrigeration, rotating machinery, building codes and building  
20 energy simulations and modeling. McCarty Decl. ¶17.

21 PG&E paid \$15 million pursuant to these and similar programs in fiscal year  
22 2000. PG&E estimates that it owes approximately \$4 million pursuant to these professional  
23 consulting programs and contract work authorizations for services rendered pre-petition,  
24 including \$900,000 in invoices already received, and \$3.1 million in expected invoices for  
25 work performed prior to the filing of the bankruptcy petition. Id. ¶18.

1 C. Low-Income Energy Efficiency Program.

2 Section 382 of the Public Utilities Code requires PG&E to fund energy efficiency  
3 programs targeting low-income<sup>10</sup> customers. In compliance with this mandate, PG&E is  
4 continuing a program that it began in 1978, which offers free weatherization to  
5 approximately 50,000 low-income homes per year. Weatherization may include the  
6 installation of attic insulation, door weather-stripping, showerheads, caulking, water heater  
7 blankets, compact fluorescent lights, faucet aerators, refrigerators and portable evaporative  
8 coolers, as well as minor home repairs and other measures. PG&E reimburses the  
9 contractors who perform marketing, education and installations under this program. In 2000,  
10 PG&E paid \$24.9 million for these programs, and still owes \$1 million in outstanding  
11 invoices for education, marketing and measure installations, and expects to receive an  
12 additional \$3.1 million in invoices for work performed prior to the filing of the bankruptcy  
13 petition. Id. ¶19.

14  
15 D. The Energy Efficiency Programs Balancing Accounts.

16 After the institution of the surcharge pursuant to the 1996 Legislation, PG&E  
17 established three separate balancing accounts for Energy Efficiency Programs funds to  
18 replace the prior balancing accounts: the Energy Efficiency Balancing Account ("EEBA"),  
19 the Public Purpose Program Efficiency Balancing Account ("PPPEBA"), and the Public  
20 Purpose Program Low-Income Balancing Account ("PPPLIBA"). The EEBA is used to fund  
21 pre-1998 Energy Efficiency Programs.<sup>11</sup> The PPPLIBA funds post-1998, Low-Income  
22 Energy Efficiency Programs, and the PPPEBA funds all of the other post-1998 regular  
23 Energy Efficiency Programs. Id. ¶21.

24 The Energy Efficiency Programs portion of PG&E's overall revenues are booked

25 <sup>10</sup>"Low-income" is defined by the Public Utilities Commission as 150% of the federal poverty guidelines for  
26 most families and 200% of the federal poverty level for senior citizens and the disabled.

27 <sup>11</sup> Since the EEBA is used to pay outstanding commitments from pre-1998 programs as payment obligations  
28 come due, no new money (other than interest on the balance in the account) is credited to this account. It is used only to  
pay old obligations.

1 to either the PPPEBA or PPPLIBA, as appropriate, where the funds (plus accumulating  
2 interest) are held until used to pay energy efficiency costs. These particular accounts are  
3 used solely for Energy Efficiency Programs funds, and to ensure that the funds collected for  
4 these programs are expended solely on these programs. All Energy Efficiency Programs  
5 expenses are paid through these accounts. If PG&E does not spend all the money collected  
6 each year for these programs, the money is rolled over with interest from year to year to fund  
7 future Energy Efficiency Programs initiatives. PG&E is not permitted to use the funds in the  
8 balancing accounts for any purposes other than the express purposes of the accounts. Any  
9 unspent funds remaining in the accounts at the end of each year are carried forward for  
10 spending in a future year. *Id.* ¶22.

11 Currently, PG&E holds approximately \$260 million in its Energy Efficiency  
12 accounts to be held and used exclusively for Energy Efficiency Programs. *Id.* ¶23.

#### 13 IV.

#### 14 ARGUMENT

15  
16 A. The Debtor Is Merely A Conduit Of The Public Purpose Programs Funds, And  
17 Such Funds Therefore Do Not Constitute Part Of The Bankruptcy Estate.

18 Section 541(d) of the Bankruptcy Code provides in pertinent part:

19 Property in which the debtor holds, as of the commencement of the  
20 case, only legal title and not an equitable interest . . . becomes property  
21 of the estate . . . only to the extent of the debtor's legal title to such  
property, but not to the extent of any equitable interest in such  
property that the debtor does not hold.

22 Because, as demonstrated at some length in Section III above, PG&E is merely a  
23 conduit for the Public Purpose Programs funds and is intended effectively to pass through  
24 those funds by ensuring that they are expended or forwarded on solely for the designated  
25 programs, PG&E has no equitable interest in such funds under Section 541(d), and PG&E  
26 therefore should be permitted (indeed, compelled) to continue to apply the funds to their  
27 legislatively mandated purposes, including the payment of outstanding pre-petition  
28 obligations owed to qualifying customers, vendors and contractors on account of the Public

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1 Purpose Programs.

2 Indeed, the one case that is remarkably factually on point reaches just such a  
3 conclusion, invoking constructive trust doctrine where the debtor, as PG&E here, merely acts  
4 as a conduit for funds. In re Columbia Gas Systems, Inc., 997 F.2d 1039, 1054 (3d Cir.  
5 1993). In Columbia Gas, the debtor, the owner of a natural gas pipeline, filed a bankruptcy  
6 petition and moved the court for permission to pay certain pre-petition obligations, including  
7 (1) refunds collected from upstream suppliers pursuant to a FERC order and owed to the  
8 debtor's customers; and (2) gas surcharges collected pursuant to federal regulations and  
9 owed to a non-profit industry research institute. The Third Circuit found that the debtor held  
10 these funds in a constructive trust and accordingly could honor pre-petition obligations  
11 pertaining to such funds.

12 The Columbia Gas court applied federal common law, which "imposes a trust  
13 when any entity acts as a conduit, collecting money from one source and forwarding it to its  
14 intended recipient." Id. at 1056 (citing In re Penn Central Transp. Co., 486 F.2d 519, 523-37  
15 (3d Cir. 1973) (en banc). The court reasoned that although many state laws require  
16 wrongdoing for the imposition of a constructive trust, "[t]he legislative history of Section  
17 541(d) makes it clear that when a debtor collects money on behalf of another this money is  
18 held in constructive trust for the eventual recipient even absent misconduct." Id. at 1056.<sup>12</sup>  
19 The court therefore found that, to the extent that "state law is inconsistent with this  
20 definition, it must be displaced." Id. Both the customer refunds and research surcharges  
21 were therefore found to be held in constructive trust. Id. at 1063.<sup>13</sup>

22 <sup>12</sup>The relevant portion of the House Report demonstrates that Congress did not intend to limit constructive trusts  
23 to money wrongfully obtained:

24 Situations occasionally arise where property ostensibly belonging to the debtor will actually not be  
25 property of the debtor, but will be held in trust for another. For example, if the debtor has incurred  
26 medical bills that were covered by insurance, and the insurance company had sent the payment of the bills  
27 to the debtor before the debtor had paid the bill for which the payment was reimbursement, the payment  
28 would actually be held in constructive trust for the person to whom the bill was owed.

H.R.Rep. No. 95-595, 95th Cong., 1st Sess. 368 (1977), reprinted in 1978 U.S.C.C.A.N. 5963, 6324.

<sup>13</sup>On the other hand, obligations to upstream gas suppliers, analogous to suppliers of electricity, were found to be  
debts of the debtor. "Since Columbia pays the upstream suppliers before it receives money from its customers,  
(continued . . . )

Similarly, in the present case, PG&E merely acts as a conduit for the Public Purpose Programs funds. PG&E collects funds that are 100% the proceeds of a special surcharge specifically identified and mandated by the California Legislature for funding the subject Public Purpose Programs, which in turn entails incurring obligations to qualifying customers, vendors and contractors, as well as the costs of administering the programs. PG&E meticulously tracks and accounts for all of the Public Purpose Programs funds via the various balancing accounts and via the required transfers to the CEC and the State Board of Equalization described in detail in Section III above, thus ensuring that all Public Purpose Programs funds are available to be expended or transferred solely for their intended purposes. Under these circumstances, there should be no doubt that PG&E is merely the conduit of the Public Purpose Programs funds and that such funds should continue to be applied to their mandated purposes regardless of whether the funds are owed on account of pre-petition or post-petition obligations.<sup>14</sup> Simply stated, the qualifying participants in the Public Purpose Programs have always been intended and designed to be the sole beneficiaries of these Public Purpose Programs funds.

B. Payment Of Pre-Petition Obligations Pursuant To The Public Purpose Programs Should Be Authorized Pursuant To Section 105 Of The Bankruptcy Code And The Court's Inherent Equitable Powers.

Section 105 of the Bankruptcy Code authorizes this Court to "issue any order, process, or judgment that is necessary or appropriate to carry out the provisions of this title."

(... continued)

Columbia does not act as a conduit or a collecting agent for the upstream suppliers." Columbia Gas, 997 F.2d at 1063.

<sup>14</sup>The CPUC, in its February 5, 2001 Decision approving the 2001 Energy Efficiency Programs, stated that "[t]he funds collected and earmarked [for the 2001 Energy Efficiency Programs] shall be held by the utilities in trust for the benefit of the commission and spent solely in accordance with the budgetary and other requirements set forth herein and shall not be used for any other purpose(s) whatsoever." The notion that Energy Efficiency Programs funds are held in trust for the benefit of the CPUC appears to be technically incorrect, since various customers, vendors and contractors are obviously the intended beneficiaries of the Energy Efficiency Programs, not the CPUC. The position taken herein that the funds collected and earmarked for the Energy Efficiency Programs (and more broadly, the funds collected and earmarked for any of the Public Purpose Programs) are effectively held in constructive trust by PG&E for the beneficiaries of the Public Purpose Programs is not based on the confusing trust language in the CPUC's February 5 Decision, but rather on the totality of the specific facts and circumstances pertaining to the surcharge for the Public Purpose Programs as detailed in Section III above.

1 The purpose of Section 105 is "to assure the bankruptcy court's power to take whatever  
2 action is appropriate or necessary in aid of the exercise of their jurisdiction." 2 Collier on  
3 Bankruptcy 105.01 at 105-6 (15th ed. rev. 2000).

4 It is essential that PG&E be allowed to carry out the Public Purpose Programs.  
5 Even if this Court for any reason were to find that the Public Purpose Program funds do not  
6 qualify as a constructive trust for purposes of Section 541(d), the California Legislature has  
7 committed to the public and the beneficiaries of these programs that the funds collected  
8 pursuant to a special surcharge on all customers' bills would be used for Public Purpose  
9 Programs encouraging energy efficiency and conservation, providing special assistance to  
10 low-income families, providing useful research and development, and encouraging  
11 environmentally beneficial renewable generation to promote these results. Customer  
12 confidence in both government and our public utilities would be seriously eroded if PG&E  
13 were required to withhold payment for obligations for these legislatively-mandated programs  
14 that have been fully funded through a special rate surcharge, and then freeze or apply these  
15 essentially public funds to other ends or purposes.

16 Moreover, in the midst of the current energy crisis, and in a market in which  
17 PG&E's wholesale cost of energy outstrips its retail rates by a multiple of seven or more,  
18 energy conservation makes supreme economic, political and social good sense. While some  
19 of the Public Purpose Programs by legislative design are geared toward mid- to long-term  
20 conservation or market transformation, many, such as the rebate and weatherization  
21 programs within the ambit of the Energy Efficiency Programs, yield immediate and  
22 significant results. Proceeding uninterrupted with the Public Purpose Programs and applying  
23 all Public Purpose Programs funds for their intended purposes makes eminent sense from  
24 both a legal and policy perspective, and, as such, can only ultimately further the goal of an  
25 effective reorganization.

26 Accordingly, if for any reason this Court determines that the Public Purpose  
27 Programs funds constitute part of PG&E's bankruptcy estate, PG&E requests that pursuant  
28 to the Court's authority under Section 105(a) of the Bankruptcy Code, the Court authorize

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1 PG&E to continue with all the legislatively mandated Public Purpose Programs, including  
2 bringing current and remaining current on all obligations to customers, vendors and  
3 contractors who qualify for payment from funds assessed and collected for the Public  
4 Purpose Programs.

5  
6 V.

7 CONCLUSION

8 For all of the foregoing reasons, PG&E respectfully requests that this Court enter  
9 an order (1) determining that PG&E is merely a conduit of the funds collected by PG&E  
10 pursuant to the Public Purpose Programs surcharge on all customers' bills, that such funds do  
11 not constitute part of PG&E's bankruptcy estate pursuant to Section 541(d) of the  
12 Bankruptcy Code, and that PG&E is therefore permitted to pay all outstanding pre-petition  
13 obligations incurred in connection with the Public Purpose Programs that are within the  
14 surcharged amounts for such programs, and otherwise to use and apply the surcharged  
15 amounts solely for the Public Purpose Programs, or (2) alternatively, pursuant to Section  
16 105(a) of the Bankruptcy Code, authorizing PG&E to continue the Public Purpose Programs  
17 uninterrupted, including, without limitation, payment of all outstanding pre-petition  
18 obligations incurred in connection with the Public Purpose Programs that are within the  
19 surcharged amounts for such programs.

20 DATED: April 24, 2001

21 Respectfully submitted,

22 HOWARD, RICE, NEMEROVSKI, CANADY,  
23 FALK & RABKIN  
A Professional Corporation

24 By:   
25 JEFFREY L. SCHAFER

26 Attorneys for Debtor and Debtor in Possession  
27 PACIFIC GAS AND ELECTRIC COMPANY  
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